

IN THE UNITED STATES DISTRICT COURT  
FOR THE NORTHERN DISTRICT OF CALIFORNIA

JOHN T. KENDALL, Chapter 7 Trustee,

No. C 07-3713 CW

Plaintiff,

ORDER TENTATIVELY  
GRANTING IN PART  
DEFENDANT'S MOTION TO  
WITHDRAW REFERENCE  
AND REQUESTING  
RECOMMENDATION FROM  
BANKRUPTCY JUDGE

v.

HARTFORD FIRE INSURANCE COMPANY,

Defendant.

Defendant Hartford Fire Insurance Co. moves to withdraw the reference to the U.S. Bankruptcy Court of Plaintiff John T. Kendall's claim against it. Plaintiff opposes Defendant's motion. The matter was taken under submission on the papers. Having considered all of the papers submitted by the parties, the Court tentatively grants Defendant's motion in part and denies it in part.

BACKGROUND<sup>1</sup>

This action arises out of a fraudulent scheme executed by Francis Reimers. In or about 1996, Reimers founded Plan Compliance

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<sup>1</sup>The facts described in this section are taken from the allegations in the complaint and the materials submitted in support of the present motion.

1 Group (PCG). PCG provided investment services on behalf of federal  
2 employees and employees of state and local educational  
3 institutions. These services included collecting and remitting  
4 money designated by employees for deposit in their personal  
5 retirement plans.

6 Reimers also held himself out as the representative of a  
7 business called Advisory Services Group (ASG), which purportedly  
8 provided financial services to individual investors. It is not  
9 known whether ASG actually existed as a separate entity. Pursuant  
10 to the fraudulent scheme, Reimers diverted funds obtained through  
11 PCG's operations to pay guaranteed monthly dividends to ASG  
12 investors and to cover his own personal expenses. In late 2005, an  
13 investigation led to the discovery that Reimers was embezzling PCG  
14 funds. Reimers subsequently plead guilty to federal criminal  
15 charges and was sentenced to nine years in prison. PCG became the  
16 subject of a voluntary Chapter 7 bankruptcy case. Plaintiff is the  
17 trustee in that action.

18 In his role as trustee, Plaintiff learned that PCG had  
19 purchased a bond from Defendant in 1999, pursuant to which  
20 Defendant agreed to pay PCG up to two million dollars for any loss  
21 resulting from theft by a PCG employee. Plaintiff sought  
22 reimbursement from Defendant for losses caused by Reimers'  
23 misappropriation of PCG funds. Defendant investigated PCG's claim,  
24 but never issued a determination on PCG's eligibility for  
25 reimbursement under the bond.

26 On May 18, 2007, Plaintiff filed an adversary complaint  
27 against Defendant in the bankruptcy proceedings. The complaint  
28

1 asserts one claim only, seeking "declaratory relief" in the form of  
2 "a declaration that under the terms of the bond, Defendant has an  
3 obligation to Plaintiff to fully and completely reimburse PGC in  
4 the amount of \$2 million in connection with Reimers' defalcations."  
5 Req. for Judicial Notice Ex. 1 at 5.<sup>2</sup> On or about June 29, 2007,  
6 Defendant filed a motion for withdrawal of the reference of this  
7 claim to the bankruptcy court. On or about July 19, 2007, the  
8 bankruptcy court transferred the motion to the district court for  
9 determination. On October 24, 2007, Defendant made its motion in  
10 the district court for withdrawal of the reference. The case was  
11 recently reassigned to the undersigned.

#### 12 DISCUSSION

13 Defendant argues that, because Plaintiff's claim against it is  
14 a non-core proceeding in which Defendant intends to demand a jury  
15 trial,<sup>3</sup> and because Defendant does not consent to a jury trial  
16 before the bankruptcy court, the Court should withdraw the  
17 reference of Plaintiff's claim to the bankruptcy court.

18 Title 28 U.S.C. § 157 classifies matters in bankruptcy cases  
19 as either "'core proceedings,' in which the bankruptcy court 'may  
20 enter appropriate orders and judgments,' or 'non-core proceedings,'  
21 which the court may hear but for which it may only submit proposed  
22 findings of fact and conclusions of law to the district court for

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23  
24 <sup>2</sup>The Court grants Defendant's request that it take judicial  
notice of the complaint filed in the bankruptcy proceedings.

25 <sup>3</sup>Defendant has not yet answered the complaint or demanded a  
26 jury trial. This order is premised on the assumption that  
27 Defendant will timely file a jury demand within ten days of its  
answer, as required by Rule 38(b) of the Federal Rules of Civil  
Procedure.

1 de novo review." Security Farms v. Int'l Bhd. of Teamsters, 124  
2 F.3d 999, 1008 (9th Cir. 1997) (quoting 28 U.S.C. § 157).

3 Claims "arising under" or "arising in" Title 11 of the United  
4 States Code are core proceedings. In re Harris Pine Mills, 44 F.3d  
5 1431, 1435 (9th Cir. 1995). A claim arises under Title 11 if it  
6 involves "a cause of action created or determined by a statutory  
7 provision of Title 11," while a claim arises in Title 11 if it is  
8 an administrative matter that arises only in bankruptcy cases. Id.  
9 (quoting In re Wood, 825 F.2d 90, 96-97 (5th Cir. 1987)). "If the  
10 proceeding does not invoke a substantive right created by the  
11 federal bankruptcy law and is one that could exist outside of  
12 bankruptcy it is not a core proceeding." Id. (quoting In re Wood,  
13 825 F.2d at 97).

14 Section 157(c)(1) requires de novo review by the district  
15 court of all non-core matters. As a result, "holding jury trials  
16 in bankruptcy court on non-core matters would necessarily result in  
17 reexamination of the jury's fact-finding, thereby violating the  
18 Seventh Amendment's prohibition on such reexamination." In re  
19 Daewoo Motor Am., Inc., 302 B.R. 308, 314 (Bankr. C.D. Cal. 2003).  
20 Thus, "bankruptcy courts cannot conduct jury trials on noncore  
21 matters, where the parties have not consented." In re  
22 Cinematronics, Inc., 916 F.2d 1444, 1451 (9th Cir. 1990).

23 Plaintiff's claim for payment pursuant to the terms of the  
24 bond is one for breach of contract under the common law. It does  
25 not "arise under" or "arise in" Title 11 because Plaintiff's  
26 substantive right to recovery was not created by the bankruptcy  
27 laws. Therefore, the claim appears to be a non-core proceeding.

1 This is true even though, as Plaintiff notes, insurance proceeds  
2 under the bond may represent the largest potentially available  
3 asset from which to pay the claims of PCG's creditors. While the  
4 potential effect of the breach of contract claim on a resolution of  
5 the matters before the bankruptcy court renders the claim "related  
6 to" the core proceedings, see In re Harris Pine Mills, 44 F.3d at  
7 1435, it does not convert the claim into a core proceeding itself.<sup>4</sup>

8 Plaintiff argues that, even if his claim is found to be a non-  
9 core proceeding, Defendant has no right to a jury trial because the  
10 claim is one for declaratory judgment and seeks equitable relief.  
11 Nonetheless, the claim appears to be fundamentally one for breach  
12 of contract, despite the fact that it is styled as one for  
13 declaratory relief and does not contain the phrase "breach of  
14 contract." A true declaratory judgment action anticipates a future  
15 lawsuit brought by the defendant against the plaintiff. It  
16 provides the plaintiff with the opportunity to establish that his  
17 or her present conduct does not give rise to liability, thereby  
18 allowing the plaintiff to carry on with that conduct without the  
19 fear of being sued by the defendant in the future. This is not the  
20 case here. Plaintiff is not trying to ward off a future lawsuit by  
21 Defendant. To the contrary, he claims that Defendant is presently  
22 in breach of its contractual obligation to reimburse PCG for its  
23 losses. Nor is the requested relief equitable in nature, despite  
24 Plaintiff's characterization of it as such; a "declaration that

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26 <sup>4</sup>The cases Plaintiff cites from the Second Circuit are not  
27 applicable here; the Ninth Circuit takes a narrower view than the  
28 Second Circuit of what constitutes a core proceeding. See In re  
Daewoo Motor, 302 B.R. at 311-12.

1 under the terms of the bond, Defendant has an obligation to  
2 Plaintiff to fully and completely reimburse PGC in the amount of \$2  
3 million" is tantamount to a money judgment.

4 Accordingly, it appears that Defendant has the right to a jury  
5 trial. Because Defendant does not consent to a jury trial before  
6 the bankruptcy court on this non-core proceeding, the trial may not  
7 be conducted in the bankruptcy court. Therefore, the Court is  
8 inclined to withdraw the reference to the bankruptcy court for the  
9 purposes of the trial of this action.

10 However, a "valid right to a Seventh Amendment jury trial in  
11 the district court does not mean the bankruptcy court must  
12 instantly give up jurisdiction and that the action must be  
13 transferred to the district court. Instead, . . . the bankruptcy  
14 court may retain jurisdiction over the action for pre-trial  
15 matters." In re Healthcentral.com, 504 F.3d 775, 788 (9th Cir.  
16 2007). Because Plaintiff's breach of contract claim is "related  
17 to" the bankruptcy proceedings in that insurance proceeds under the  
18 bond may represent PCG's largest available asset, the interest of  
19 judicial economy would likely favor a resolution of all pre-trial  
20 matters in the bankruptcy court, which is already familiar with the  
21 background of this case. Accordingly, the Court is inclined to  
22 withdraw the reference only after the bankruptcy court has  
23 adjudicated all pre-trial matters.

24 However, the Court requests the bankruptcy court's  
25 recommendation on this matter, and will refrain from issuing a  
26 final order on this motion until the bankruptcy court has had an  
27 opportunity to provide such a recommendation.

CONCLUSION

For the foregoing reasons, the Court tentatively GRANTS IN PART and DENIES IN PART Defendant's motion to withdraw the reference to the U.S. Bankruptcy Court. The Court is inclined to withdraw the reference, but only after the bankruptcy court has adjudicated all pre-trial matters. The Court will enter a final order after the bankruptcy court has had an opportunity to issue its recommendation.

IT IS SO ORDERED.

Dated: 3/19/08



CLAUDIA WILKEN  
United States District Judge